

# **AUDITOR'S REPORT OF THE AUDITOR-GENERAL TO THE KWAZULU-NATAL PROVINCIAL LEGISLATURE AND THE COUNCIL ON NQUTHU MUNICIPALITY**

## **REPORT ON THE FINANCIAL STATEMENTS**

### **Introduction**

1. I have audited the accompanying financial statements of the Nquthu Municipality, which comprise the statement of financial position as at 30 June 2010, and the statement of financial performance, statement of changes in net assets and cash flow statement for the year then ended, a summary of significant accounting policies and other explanatory information, as set out on pages 7 to 44.

### **Accounting officer's responsibility for the financial statements**

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and in the manner required by the Local Government: Municipal Finance Management Act of South Africa, 2003 (Act No.56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2009 (Act No.12 of 2009) (DoRA). This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

### **Auditor-General's responsibility**

3. As required by section 188 of the Constitution of South Africa, 1996 (Act No. 108 of 1996), section 4 of the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and section 126(3) of the MFMA, my responsibility is to express an opinion on these financial statements based on my audit.
4. I conducted my audit in accordance with International Standards on Auditing and *General Notice 1570 of 2009* issued in *Government Gazette 32758 of 27 November 2009*. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
5. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
6. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

## **Basis for qualified opinion**

### **Consumer debtors and impairment**

7. Included in non-interest bearing consumer debtors of R15,692 million, in note 11 to the financial statements is an amount of R9,342 million relating to a bad debt impairment. This impairment was based on a general provision of 60 percent of the consumer debtors outstanding at year-end, without being supported by a reasonable bases and assumptions and in this regard, the accounting officer did not comply with South African Statement of Generally Accepted Accounting Practice, IAS 39 (AC 133), *Financial Instruments: Recognition and Measurement*. Moreover, these debtors were not discounted to take into consideration the impact of the time value of money emanating from deferred settlement terms. Consequently, I did not obtain sufficient appropriate evidence through alternative procedures to satisfy myself as to the valuation of consumer debtors and the related impairment loss.

### **Landfill site**

8. At the date of my report, the accounting officer was still in the process of gathering information on the cost, depreciation, impairment and the associated provision for rehabilitation of the solid waste disposal landfill site in order to comply with SA Standards of GRAP 17, *Property, plant and equipment* and GRAP 19, *Provisions, contingent liabilities and contingent assets*. Therefore, I was unable to obtain sufficient and appropriate audit evidence as to the valuation of the landfill site and the rehabilitation provision, as well the impact of the non-recognition on 2008-09 corresponding financial statement amounts.

## **Qualified opinion**

9. In my opinion, except for the possible effects of the matters described in the Basis for qualified opinion paragraphs, these financial statements present fairly, in all material respects, the financial position of the Nquthu Municipality as at 30 June 2010 and its financial performance and its cash flows for the year then ended in accordance with the SA Standards of GRAP and in the manner required by the MFMA and DoRA.

## **Emphasis of matters**

10. I draw attention to the matters below. My opinion is not modified in respect of these matters:

### **Restatement of corresponding figures**

11. As disclosed in note 3 to the financial statements, the corresponding figures for 2008-09 have been restated as a result of an error discovered during 2009-10 in the financial statements of the Nquthu Municipality at, and for the year ended, 30 June 2009.

### **Material electricity distribution losses**

12. As disclosed in note 36 to the financial statements, electricity distribution losses to the amount of R1,061 million were incurred. The reason for these losses are currently under investigation.

### **Additional matter**

13. I draw attention to the matter below. My opinion is not modified in respect of this matter:

### **Unaudited supplementary schedules**

14. The supplementary information set out on pages 45 to 55 does not form part of the financial statements and is presented as additional information. I have not audited these schedules and accordingly I do not express an opinion thereon.

### **REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS**

15. As required by the PAA and in terms of *General Notice 1570 of 2009* issued in *Government Gazette 32758 of 27 November 2009*, I include below my findings on the report on predetermined objectives, compliance with the following key laws and regulations (MFMA) and financial management (internal control).

### **Predetermined objectives**

16. Material findings on the report on predetermined objectives, as set out on pages XX to XX, are reported below:

### **Non-compliance with regulatory and reporting requirements**

#### **Inadequate content of integrated development plan**

17. The integrated development plan (IDP) of the Nquthu Municipality did not include the key performance indicators and performance targets determined in terms of its performance management system, as required by sections 26(i) and 41(1) (b) of the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA) and regulation 12 of the Municipal Planning and Performance Management Regulations, 2001(MPPMR).

#### **Service delivery and budget implementation plan not approved timeously**

18. The Nquthu Municipality did not comply with section 53(1)(c)(ii) of the MFMA, as the service delivery and budget implementation plan (SDBIP) was not approved within the prescribed time frame of 28 days after the budget was approved.

#### **Existence and functioning of a performance audit committee**

19. The Nquthu Municipality did not appoint and budget for a performance audit committee, nor was another audit committee utilised as the performance audit committee, as required by regulation 14(2) of the MPPMR.

#### **Usefulness of reported performance information**

The following criteria were used to assess the usefulness of the planned and reported performance:

- Consistency: Has the municipality reported on its performance with regard to its objectives, indicators and targets in its approved IDP, i.e. are the objectives, indicators and targets consistent between planning and reporting documents?
- Relevance: Is there a clear and logical link between the objectives, outcomes, outputs, indicators and performance targets?
- Measurability: Are objectives made measurable by means of indicators and targets? Are indicators well defined and verifiable, and are targets specific, measurable, and time bound?

- The following audit findings relate to the above criteria

### **Planned and reported performance targets not specific, measurable, and time bound**

20. For the selected objectives (access to housing and land, poverty and public participation), 100% of the planned and reported targets were not:

- specific in clearly identifying the nature and the required level of performance;
- measurable in identifying the required performance; and
- time bound in specifying the time period or deadline for delivery.

### **Reported performance information not consistent**

21. Performance objectives, key performance indicators and targets were not aligned between the municipalities IDP, SDBIP, budget and the municipality's scorecard.

### **Reliability of reported performance information**

The following criteria were used to assess the usefulness of the planned and reported performance:

- **Validity:** Has the actual reported performance occurred and does it pertain to the entity i.e. can the reported performance information be traced back to the source data or documentation?
- **Accuracy:** Amounts, numbers and other data relating to reported actual performance has been recorded and reported appropriately.
- **Completeness:** All actual results and events that should have been recorded have been included in the reported performance information.

The following audit findings relate to the above criteria:

### **Controls for source data not appropriately designed**

22. Reported information with regard to the indigent register was not reliable due to the application forms not being pre-numbered and approved, in all instances.
23. No follow-ups relating to the land proclamation and formalisation were performed on a monthly basis and a register was not maintained to track progress in this regard, in all instances.

## **Compliance with laws and regulations**

### **Local Government Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA)**

#### **Non-adherence to legislation**

##### **The audit committee was not functioning properly**

24. Contrary, to sections 166(2)(a)(b) and (v), the audit committee did not adequately discharge its mandated responsibilities.

##### **The accounting officer did not adhere to his statutory responsibilities**

25. Risk assessments were not performed annually, a fraud prevention plan was not developed, and a disaster recovery plan was not in place, as required by section 62(1)(c).
26. Contrary, to sections 63(1) (a) and (b) an asset maintenance plan was not developed.
27. The financial statements and the annual performance report was not submitted for auditing within two months after year-end, in contravention of section 126(1)(a).

## **INTERNAL CONTROL**

28. I considered internal control relevant to my audit of the financial statements and the report on predetermined objectives as well as compliance with the following key laws and regulations (MFMA) but not for the purpose of expressing an opinion on the effectiveness of internal control.
29. The matters reported are limited to the significant deficiencies that gave rise to the basis for qualified opinion paragraph, the findings on the report on predetermined objectives and the findings on compliance with laws and regulations.

## **Leadership**

30. The leadership did not exercise adequate oversight over operational aspects to improve financial, compliance and performance reporting because decisive actions had not been taken to mitigate avoidable risks through the implementation of timely corrective measures. Moreover, the importance of compliance with financial and performance reporting requirements was not adequately emphasised.

## **Financial and performance management**

31. Although record-keeping and systems have improved, the quality of reporting was not at desired levels, as evidenced from the material corrections in amounts and disclosures in the financial statements and the errors on the reported findings on performance management.

## **Governance**

32. The audit committee and internal audit function did not adequately discharge their mandated responsibilities, thus impacting on the reliability of internal controls related to financial and performance reporting. Moreover, the accounting officer did not ensure that a fraud prevention plan was in place, coupled by the performance of annual risk assessments.

## **OTHER REPORTS**

### **Investigations**

#### **Investigations completed during the financial year**

33. An investigation was conducted on the request of the municipality based on the allegation of misappropriation of assets by the previous mayor. The investigation has resulting in criminal proceedings being instituted for the recovery of an amount of R224 709 in this regard.

Pietermaritzburg

30 November 2010



**AUDITOR - GENERAL**  
**SOUTH AFRICA**

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